Switching	Capacity charge for line-specific costs plus usage sensitive charge based on calling volumes.
Operator systems	Capacity charge for non-usage sensitive costs plus charge per message for usage sensitive costs.
Common transport	Usage sensitive charge.
Tandem switching	Usage sensitive charge.
Signaling links	Capacity charge for costs attributable to links dedicated to carrying signaling to/from an ALEC switch/STP/SCP; usage sensitive chages (per query) for "common" links between ILEC switches, STPs/SCPs.
Signal transfer point	Capacity charge for terminations of dedicated signaling links; usage sensitive charge for terminations of "common" signaling links; usage sensitive charge for signaling query "switching."
Service control point	Capacity charge for terminations of dedicated signaling links; usage sensitive charge for terminations of "common" signaling links; usage sensitive charge for costs of processing signaling queries.

The Commission also seeks comment on whether to adopt rules for pricing of "shared access" facilities. NPRM ¶153. The Commission should prescribe a rule allowing accessing carriers at their election to obtain rates based on capacity, not volume. This option, when coupled with the right of resale inherent in the offering of unbundled elements to carriers, will avoid the need for prescription of complex cost attribution or allocation rules for volumetric pricing: resale and arbitrage will limit volumetric charges to competitive levels.

D. The Commission Should Implement And Clarify The Act's Price Discrimination Prohibitions.

Sections 251 and 252 of the 1996 Act expressly prohibit discriminatory network element and interconnection rates. See NPRM ¶155. The ILECs' existing monopoly control of local exchange facilities make these nondiscrimination requirements critical to the competitive functioning of exchange and interexchange markets. The Commisison should therefore confirm that a discount or other arrangement that is practically available only to the ILEC (including its affiliates), or is otherwise structured to favor the ILEC, is unlawful under the nondiscrimination provisions of the 1996 Act.

E. The Commission Should Mandate Symmetrical TSLRIC-Based Reciprocal Compensation With An Interim Bill-And-Keep Solution.

The Commission should move toward the establishment of rules requiring the payment of reciprocal compensation that is symmetrical, with payments in each area based on the ILEC's TSLRIC of terminating traffic in that area. This approach will provide carriers with the proper incentives to minimize costs and has the added benefit of being administratively manageable given that ILECs will already be performing TSLRIC studies.

Reciprocal compensation arrangements will not become practical, however, until mechanisms are developed to measure the relevant terminating traffic volumes. In the interim, the Commission should prescribe "bill and keep" arrangements. ILECs should have the opportunity to switch to reciprocal compensation in an area once they can measure traffic and TSLRIC costs have been determined.

F. Any And All Subsidies Must Be Independent Of, And Not Allowed To Distort, The Efficient Economic-Cost-Based Rates Necessary To Effective Implementation Of The Act.

It is critical that cost-based charges for unbundled network elements, interconnection, and collocation not be corrupted by subsidies or other non-cost-based "add-ons." Accordingly, all subsidies -- i.e., whatever other amounts the Commission, the states or the Joint Board may determine that ILECs should be paid, whether to benefit consumers or the ILECS themselves -- should be recovered through competitively neutral separate charges.

1. Universal Service Subsidies Designed To Benefit Consumers.

Universal service costs or subsidies have no place in rates for interconnection or unbundled network elements -- Sections 251 and 252 require that those rates reflect the costs of providing those network elements, not the costs of implementing other social policies. Accordingly, network element and interconnection rates should exclude universal service costs or subsidies, and those costs should be recovered through the New Universal Service Fund.

2. "Subsidies" Designed To Benefit ILECs.

Certain ILECs incorrectly claim an entitlement to "subsidies" designed to guarantee them recovery of some or all of the revenues they would have earned under the state and federal rate regulations that Congress abandoned in the Act and replaced with economic-cost-based ratemaking. Those claims are exaggerated and otherwise meritless.

There is no legal or policy basis for reimbursing the ILECs for any revenue "shortfalls" that may arise after the Commission's rules requiring economic-cost-based pricing for network elements and access are implemented. As noted above, TSLRIC rates are compensatory. For that and other reasons, it is settled law that such rates are in no way confiscatory.[103] Further,

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[103] The Constitution requires only that the "end result" of rate regulation be just and reasonable. See FPC v. Hope Natural Gas Co., 320 U.S. 591 (1944). There can be no constitutional claim under this standard, unless the agency's rate methodology produces rates as a whole that are so low that they "jeopardize the financial integrity of the [regulated] companies, either by leaving them insufficient operating capital or by impeding their ability to raise future capital." Duquesne Light Co. v. Barasch, 488 U.S. 299, 312 (1989). By definition, TSLRIC, which allows regulated companies to recover all of the forward-looking costs of providing network elements -- including the cost of attracting capital -- is sufficient to allow those companies to attract capital. See also Market St. Ry. v. Railroad Comm'n, 324 U.S. 548, 567 (1945) (the Fifth Amendment "has been applied to prevent governmental destruction of existing economic values. It has not and cannot be applied to insure values or to restore values that have been lost by the operation of economic forces"). It is equally clear that the ILECs have no constitutional entitlement to recovery of their

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the 1996 Act requires that rates reflect the economic cost of providing network elements and interconnection and does not authorize "add-ons" that have nothing to do with economic costs. Revenue "shortfalls" based on backward-looking measures of ILEC expenditures plainly are not forward-looking economic costs of providing a network element. Accordingly, at least one RBOC has recognized that "[t]o the extent [such] residual costs do not reflect forward-looking costs, clearly such costs may not be recovered under Section 252(d)(1)."[104]

Nor are there any legitimate "equity" arguments for such transfer payments to the ILECs. Much of the "shortfall" at issue merely reflects overearnings, inefficiencies, and strategic investments in facilities not needed to provide basic telephony services. Any remainder reflects the risks that all firms that make capital investments face from competition and changing technology.[105]

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actual historical expenditures. See, e.g., Illinois Bell Tel. Co. v. FCC, 988 F.2d 1254, 1263 (D.C. Cir. 1993) (Commission has no obligation "to include in the rate base all actual costs for investments prudent when made"); Second Report and Order, First Order on Reconsideration, and Further Notice of Proposed Rulemaking, Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992, 1996 FCC LEXIS 372, at *46 (FCC Jan. 26, 1996) (Commssion has "no constitutional duty to ensure full recovery" of all costs).

[104] Ameritech Ex Parte at 10.

[105] To remain competitive, companies often must write down (or write off) assets well before the end of their physical, regulatory, or accounting lives. AT&T, for example, experienced this in the 1980s when it replaced much of its analog plant with digital plant. The resulting asset writedown was borne by shareholders, and an "entitlement" due to competition was neither requested from regulators nor expected. See, e.g., Comments of Sprint Corporation, FCC Dkt Nos. DA 93-481 and 95-484, Petition for a Declaratory Ruling and Related Waivers to Establish a New Regulatory Model for the Ameritech Region, pp. 18-19 (submitted May 16, 1995).

Further, there can be no argument that ILECs or their investors -- particularly ILECs operating under price cap or other incentive regulation plans -- have any legitimate expectations of guaranteed recovery of all expenditures, as state commissions and the ILECs themselves have recognized. See, e.g., Order, Application of BellSouth for Alternative Regulation (Consumer Price Protection Plan), Dkt. No. 95-720-C, slip op. at 16, 26-27 (S.C. PUC Jan. 30, 1996) (incentive regulation

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Further, although a variety of large "shortfall" numbers have been bandied about, no immediate "shortfall" will, in fact, arise from TSLRIC pricing of network elements. On Day 1 the ILECS will earn the same revenues they earn today because the ILECs begin with virtually all retail customers, and will not even begin to lose any retail revenues (to be replaced by wholesale revenues) until AT&T and others begin the slow process of buying network elements, building platforms, marketing their services, and attempting to attract customers with lower prices and better service. Nor is there likely to be any immediate reduction in access revenues if, as the Commission appears inclined, access reform is to be delayed.[106]

In any event, the Commission should not under any circumstances let speculation about potential ILEC revenue declines interfere with the move to economic-cost-based rates

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"unhook[s]" the connection between investment and recovery of investment via rate of return revenue requirements, requires the LEC to be more efficient, and shifts the costs of new technologies from customers to shareholders); New York Public Service Commission, "NYPSC Adopts Framework Accelerating Local Telephone Competition -- More Consumer Choices: Market Opportunities" (Jan. 18, 1996) (summary attachment)(denying recovery of "stranded revenues" to companies operating under "incentive regulation plans, such as New York Telephone and Rochester Telephone, [that] have accepted the risk of recovery of stranded revenue requirement"); NARUC Staff Subcommittee on Communications, Local Competition Work Group Summary Report 52-53 (1996) (recommending that companies operating under price cap regulation not be allowed to recover stranded investment costs); BellSouth Corporation, Securities and Exchange Commission Form 10-K, Annual Report at 34 (Dec. 31, 1995) (reporting writedown of $2.7 billion because "it is doubtful that regulated rates sufficient to recover the net book value of telephone plant could be charged to and collected from customers due to expected levels of future competition").

106 Further, any equity-based "shortfall" claim should account for the ILECs' substantial past overrecoveries. Since the advent of interstate price caps, for example, the ILECs have received almost $8 billion in excess revenues. See generally MCI Comments, Preliminary Rate of Return Inquiry, Dkt. No. AAD 96-28 (March 11, 1996); AT&T Comments, CC Dkt. No. 94-1 at Appendix D (May 9, 1994).

necessary for workable competition. Thus, if the Commission nonetheless determines that a transfer payment tied to some portion of current industry revenue levels is appropriate, a competitively neutral funding and distribution mechanism that will not distort competition can be designed as a transition, rather than abandoning the essential TSLRIC basis for pricing.

IV. THE COMMISSION SHOULD ADOPT RULES ENSURING THAT ILECS COMPLY WITH THEIR OBLIGATIONS TO MAKE SERVICES AVAILABLE FOR RESALE AT WHOLESALE RATES.

Section 251(c)(4)(A) of the Act requires every ILEC "to offer for resale at wholesale rates any telecommunications service that the carrier provides at retail to subscribers who are not telecommunications carriers." Section 251(c)(4)(B) flatly prohibits ILECs from imposing "unreasonable or discriminatory conditions or limitations" upon "the resale of such telecommunications services." In enacting these provisions, Congress clearly recognized that commercially viable resale opportunities are vital to the development of competition in the local exchange.

Resale opportunities are critically important, both as a means quickly to bring at least some of the benefits of competition to consumers and as a springboard to facilities-based entry. Resellers utilize many of their own inputs, including customer service and end-user billing and marketing, to meet customer demand, and these inputs may be provided more efficiently by resellers than ILECs. Further, resale places additional pressure on the ILECs to price their services rationally to minimize the ability of new entrants to engage in price arbitrage. In addition, resale permits new entrants to compete in high-cost areas and for low income subscribers through the implicit flow-through of universal service funds received by the ILEC and incorporated into retail and wholesale rates as defined by Section 252(d)(3).

More fundamentally, resale enables competitors to establish a presence in the market and begin to win customers.[107] In view of the significant entry barriers to the

[107] See Baumol, Ordover & Willig Aff., ¶18.

provision of local exchange service, including the ILECs' entrenched positions and the need for new entrants to incur enormous sunk costs to replicate network facilities, regulatory rules that prudently minimize the risk exposure and capital requirements associated with the development of local exchange competition will serve the public interest.[108] As in the interexchange market, resale can provide a starting point for a competitive local exchange market in which an increasing number of facilities-based providers ultimately vie with each other for residential and business end users. In short, commercially viable resale is the first step in establishing a competitive market for local service.

A. The Commission Should Confirm That ILECS May Not Restrict The Services Available For Resale Or Discriminate In Favor Of Their Own Retail Operations.

Against this background, the NPRM (¶175) seeks comment on what services should be subject to resale, and what conditions or limitations an ILEC may place on resale. The plain language of Section 251(c)(4) mandates that ILECs make available for resale at wholesale rates any telecommunications service that they provide to a non-carrier subscriber. Moreover, because Congress appreciated the threat to incipient local competition posed by ILECs seeking to protect their existing monopolies, the 1996 Act also prohibits ILECs from imposing unreasonable or discriminatory conditions or limitations on resale. In order to

[108] In 1994, the Regional Bell Operating Companies had more than $210 billion invested in their local networks. Federal Communications Commission, 1994 Statistics of Communications Common Carriers, Table 2.7, at 28. By contrast, AT&T's total investment in its network as of 1994 was only $24.5 billion. Id. at 26. The investment required for a new entrant to provide more than nominal facilities-based competition in local services would be enormous. AT&T estimates that it would cost in excess of $29 billion to build facilities that could serve only the 20 percent of customers located in the most densely-populated areas of the country.

ensure that Congress' goals are realized, the Commission should confirm that ILECs are required as a matter of law to make available for resale every telecommunications service they provide to end-users.

1. ILECs Must Make Available For Resale Any Telecommunications Service That They Provide At Retail To Non-Carrier Subscribers.

Notwithstanding the plain and unambiguous language of the Act, and Congress' desire to introduce resale competition for every telecommunications service provided by ILECs to end-users, several ILECs are attempting to evade their obligations by narrowly defining the services that must be made available for resale,[109] or by "withdrawing" services which they then continue to provide on a "grandfathered" basis.[110] In Wisconsin, for example, despite a request by the State commission staff, Ameritech has not identified the services it will make available for resale. Instead, Ameritech states that it will offer for resale an "initial set of services" (currently undisclosed), and consider making additional offerings available for resale

[109] Ameritech has taken the position that it need not make the following services available for resale: service packages; promotional offerings; "grandfathered" services; "sunsetted" services; and "proprietary" services. AT&T Communications of Illinois, et al., Illinois Commerce Comm'n, Dockets 95-0458, 95-0531, Supplemental Direct Testimony of J. Thomas O'Brien, at 7-10. BellSouth has filed a tariff in Louisiana that prohibits resale of all promotional and custom or contract service arrangements.

[110] In anticipation of or in response to passage of the Act, BellSouth and U S WEST attempted to withdraw and "grandfather" their Centrex services so that they arguably did not have to offer such services for resale. U S WEST candidly admits that its purpose was to prevent resale. See Transmittal from U S WEST to the Minnesota Public Utilities Commission dated February 5, 1996 re CENTRON Services Grandparenting, p. 2 ("Continued offering of the current products to new customers in the evolving competitive environment provides arbitraging opportunities that may advantage some service providers while disadvantaging others").

based on receipt of a bona fide request.[111] Moreover, Ameritech asserts that many of its services -- such as operator services -- "do not constitute 'telecommunications services' under the 1996 Act," and that Ameritech therefore "[is] not obligated to offer them at wholesale rates."[112]

The positions taken by Ameritech and other ILECs underscore the need for the Commission to confirm that the ILECs' resale obligation applies to "any" telecommunications service offered to non-carrier customers, whether business or residential, tariffed or non-tariffed, generic or customized.[113] The 1996 Act does not recognize any exception to this requirement, presumably because to do so would effectively preclude resale competition for

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[111] Public Service Comm'n of Wisconsin, Docket 05-TI-38, Reply Brief of Ameritech Wisconsin, Resale Attachment at 4 (filed May 2, 1996). Bell Atlantic and GTE also refuse to disclose the services that they are willing (or, more accurately, are obligated) to make available for resale.

[112] Id. at 3. Ameritech Wisconsin also takes the position that its obligation to offer service for resale at a wholesale rate excludes not only trial or promotional offerings, but also individual "rate elements," as well as "pricing plans." Id. The ILECs' resale strategy appears to be: (1) don't offer a service for resale unless someone asks; (2) if a request is received, argue that the service is not a "telecommunications service"; (3) if the service is found to be a telecommunications service, relabel it a promotion or "pricing plan" and refuse to make it available to resellers; and (4) if all else fails, withdraw the service and "grandfather" existing customers.

[113] The Commission should also state explicitly that the telecommunications services ILECs must offer for resale include, but are not limited to: business services; residential services; flat-rated services; measured services; promotional and discounted services; CLASS features (such as Caller ID); Centrex; ISDN; Lifeline services; special, dedicated and switched access (to the extent offered to non-carriers); telecommunications relay service; public access line service; 911 services; individual customer basis (ICB) services; contract services, and non-tariffed (or detariffed) telecommunications services. Moreover, the Commission should make clear that states can identify other ILEC services that must be offered for resale at wholesale rates.

customers of that service, contrary to Congress' objectives.[114] The Act's requirement that all services provided by an ILEC to non-carrier customers be made available for resale likewise prevents an ILEC from evading its obligation by "withdrawing" a service except as to "grandfathered" customers. Because such an ILEC is continuing to "provide" such a service in that circumstance, the resale obligation continues to apply.[115] The Commission should therefore confirm the obligation of every ILEC to make available for resale at wholesale rates any telecommunications service it provides to new and existing non-carrier customers. Finally, to ensure that ILECs comply with their resale obligations, the Commission should require that they disclose through tariffs (or some other reporting mechanism prescribed by the state) all of their offerings or arrangements to provide telecommunications services to non-carrier customers.

2. ILECs Are Prohibited From Imposing Unreasonable Or Discriminatory Restrictions On Resale.

The plain language of the Act prohibits ILECs from imposing "unreasonable or discriminatory restrictions or limitations" on the resale of services provided to non-carrier

[114] In order to comply with their resale obligations -- as well as with the nondiscrimination requirements -- ILECs must be required, at a minimum, to offer the corresponding wholesale service simultaneously with the introduction of any new retail telecommunications service.

[115] An ILEC may still seek to evade its resale obligation by withdrawing a service without "grandfathering" existing customers. The Commission should clarify that states, consistent with their jurisdiction over retail services, may adopt rules to address this situation. In all events, the very real possibility that an ILEC may choose to withdraw or alter its retail services as a means to evade its resale obligations underscores the shortcomings of any approach that limits an entrant to resale of the ILEC's retail offering, and the importance of the requirement imposed by Section 251(c)(3) that ILECs make available a platform of network elements that entrants can use to create and offer their own services.

customers. Moreover, the Commission correctly has observed that restrictions and conditions on the resale of local services by new entrants would be contrary to the pro-competitive thrust of the Act and would likely be evidence of an exercise of market power by ILECs. AT&T therefore agrees with the Commission's tentative conclusion that "the range of permissible restrictions should be quite narrow."[116]

The 1996 Act contemplates only one permissible restriction on resale -- a state commission may restrict the resale of a service obtained at wholesale rates to the same category of customers who receive the ILEC's retail service, so long as such restriction is consistent with regulations prescribed by the Commission[117] The Commission correctly observes that this exception to the rule of unrestricted resale was intended to apply to the resale of services which receive an explicit subsidy, e.g., Lifeline services, to benefit a limited and specifically defined group of customers. NPRM, ¶176.[118] Even here, the Act prohibits an ILEC from flatly refusing to offer Lifeline service for resale. Instead, a new entrant should be able to purchase the Lifeline service at a wholesale discount (with the ILEC receiving the underlying universal service fund subsidies), but could be restricted by a state commission

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116 NPRM ¶175; see also id. at ¶197 ("We believe that few, if any, conditions or limitations should be permitted.").

117 For this and other reasons, the Commission should adopt rules, and exercise its preemption duty and authority, firmly to avoid or prohibit the anticompetitive effects of state laws, like the recent Public Utility Regulatory Act in Texas (Tex. Rev. Civ. Stat. Ann. Art. 1446c-0 (WestSupp. 1996)), which are designed or will operate to cripple or foreclose resale competition.

118 Notwithstanding the language of the Act, Bell Atlantic has filed tariffs in its region which impose blanket category-to-category restrictions on the availability of its services. The Commission's order in this proceeding should preclude such restrictions.

from reselling the Lifeline service to end-users who are not eligible for Lifeline service.[119] Aside from this limited exception for services receiving explicit subsidies, no customer or use restrictions should be permitted.[120]

Section 251(c)(4) requires that services offered for resale be provided free of any "unreasonable or discriminatory conditions or limitations." At a minimum, this means that an ILEC cannot discriminate against resellers and in favor of its own retail operations. The Commission's rules should confirm that, as part of its obligations to make services available for resale without discriminatory limitations or conditions, an ILEC must take all reasonable steps to make available operational interfaces ensuring that the service provided to resellers will be at parity with that which the ILEC provides to its own retail operations.

Such interfaces are at least as important for resale as they are when new entrants purchase unbundled network elements.[121] ILECs should be required to provide electronic

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[119] The claims of some ILECs (e.g., Bell Atlantic) that they are not required to provide a wholesale rate on services that are actually or allegedly priced "below cost" are foreclosed by the terms of the Act, and otherwise unfounded. As noted above, for customers served by resellers under Section 251(c)(4), the ILEC will be regarded as the "Eligible Carrier" and receive the subsidy created under Section 254 to fund the below-cost rates. More fundamentally, there is no conceivable basis for relieving the ILEC of an obligation to provide a discount that reflects the costs it will avoid. By definition, the ILEC receives the same net revenue whether it acts as a retailer or wholesaler.

[120] In addition, the Commission should confirm that ILECs may not condition the statutory right of an ALEC to resell services on a commitment by the reseller to construct its own network, or to serve only a particular number or percentage of its customers through resale. Nor may an ILEC deny a resale request based on a reseller's lack of state certification, the ILEC's perception of the reseller's ability to provide service, or other factors relating to the qualifications, status or identity of the reseller. It would not be appropriate for an incumbent to "police" its competitor's compliance with state law.

[121] The lack of necessary electronic interfaces has been, and continues to be, a key factor in AT&T's inability to provide viable resale competition in Rochester, NY. See Part II, supra.

interfaces for ordering, provisioning, maintenance and billing at the same level of quality, and within the same intervals, as they do for their own end-user customers.[122] To the extent an ILEC's services benefit from real-time support capabilities (such as number assignment or scheduling of repair and installation service), the interfaces provided to resellers should provide such real-time capabilities as well, so that resellers can provide equivalent support to their customers. To meet its nondiscrimination obligation, an ILEC should be required to provide operational interfaces in such a manner that a reseller's customers would not perceive a difference between the service provided by the ILEC and that provided by the reseller. NPRM, ¶91.[123]

B. The Commission Should Issue National Rules Governing The Determination Of Wholesale Rates Under The 1996 Act.

No factor will be more critical in determining whether resale will permit viable entry into the local service market than the wholesale rates at which such services are made

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[122] For a detailed discussion of the required interfaces, see Part II.D, supra. As AT&T there explains, the required interfaces can be developed using gateways that provide the necessary functionality without compromising customer (or ILEC) proprietary information and without implicating the CPNI restrictions contained in Sections 222(b) and 222(c) of the Act.

[123] Bell Atlantic is unlawfully conditioning the resale of its local service on AT&T's agreement to resell Bell Atlantic's operator services. Further, Bell Atlantic insists that the operator services resold by AT&T be branded as "Bell Atlantic." The Commission should, therefore, consider adopting a rule requiring that resellers be permitted to provide their own operator services in conjunction with resale of the ILEC's local service (at a wholesale rate that excludes the ILEC's cost of providing its own operator services). This would preclude claims by Bell Atlantic and other ILECs that they are not required to permit resale of local service without the ILECs' operator service, and promote customer choice. The Commission should also consider adopting a rule requiring ILECs to comply with reasonable requests by ALECs to brand resold services as those of the ALEC (or at least provide unbranded services). The branding rule is necessary not only to promote competition, but also to prevent customer confusion.

available. AT&T's experience in Rochester, New York demonstrates that the mere legal ability to provide resold services is meaningless unless new entrants can offer and market such service to local customers on an economically viable basis.[124] As Chairman Hundt has stressed in connection with international competition:

> Competition on paper does not count. Only competition in the market counts. A market can proclaim itself open or competitive, but whether it is or not depends upon access charges, interconnection, numbering schemes and the like.[125]

The Commission has the authority under the Act to establish the definitions and standards necessary to calculate wholesale rates. NPRM, ¶¶117, 178. In order for viable resale competition to develop and be sustained, the Commission must exercise that authority and issue detailed national rules to guide the determinations of wholesale rates.

1. Retail Rates.

Section 252(d)(3) requires that ILECs' wholesale rates be based on "retail rates charged to subscribers for the telecommunications service requested," excluding the portion thereof attributable to costs that will be avoided by the ILEC. The plain language of the Act requires that the "retail rates" to which wholesale discounts will be applied are the rates "charged to subscribers." The rates "charged to subscribers" are the rates that subscribers actually pay, not a "base" rate, "standard" rate or any other rate component, and thus include any applicable discounts, regardless of amount, type (e.g., term, volume, geographical, or

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[124] RTC offered a wholesale discount of only five percent, which is far below the level that AT&T would need to cover its retail costs. Because it was sustaining substantial losses as a reseller of local service, AT&T has ceased active marketing of its local service in Rochester.

[125] Statement before the House Commerce Subcommittee on Commerce, Trade and Hazardous Materials, March 3, 1995 at 9.

time-of-day discounts) or duration (e.g., promotional discounts).[126] Any attempt by an ILEC to exclude promotional or other discounted rates as the starting point for application of wholesale discounts -- or to exclude such offers from resale altogether -- would thus contravene the express language of the Act.

The Act does not permit exclusion of discounted or other promotional offers for good reason. If an ILEC could lawfully restrict application of the wholesale discount to the "standard" retail rate, the ILEC could put new entrants in a price squeeze that would stifle incipient competition merely by offering discounted or promotional services to its best customers.[127] Indeed, as Ameritech Wisconsin's position demonstrates, an ILEC could easily evade its resale obligations by claiming that particular offerings are "pricing plans" that are not subject to resale. This is contrary to both the letter and spirit of the 1996 Act.

2. Avoided Costs.

Section 252(d)(3) defines the wholesale rate paid by resellers as the rate charged to end users less the "marketing, billing, collection, and other costs that will be avoided" by the ILEC.[128] Congress -- and the 1996 Act -- plainly anticipate that the resulting wholesale

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126 As the retail rate changes, the wholesale discount must be applied to each currently effective retail rate.

127 Many states, such as Arizona, California, Kansas, Maryland, Missouri, Ohio, Pennsylvania, Texas, and Washington, permit promotions of at least one year in length.

128 In this regard, the NPRM (¶62) speculates that ILECs also may "offset" against their "avoided costs" those expenses that they incur to provide wholesale services. This is contrary to the plain language of the Act, which permits no such offsets. Had Congress intended a different result, it could easily have said so by expressly authorizing "offsets." A contrary reading of the statute, moreover, would jeopardize the prospects of commercially viable resale, and create frequent and complex disputes regarding the existence and amount of claimed "offsets." Finally, because all local service customers will benefit from the introduction of

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discount will be of sufficient magnitude to permit viable competition with the ILEC by an equally efficient resale competitor. The Act thus requires ILECs to extract as "avoided costs" at least all costs that should reasonably be avoided in providing the wholesale function.[129] These avoided costs include all direct costs associated with the ILEC's retail operations,[130] plus that portion of the ILEC's shared, common and general overhead costs which is associated with the ILEC's provision of its own retail service.[131]

The particular method by which wholesale discounts are determined and applied (e.g., as an overall discount across all services, by categories of services, or on a service-by-

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local service competition, it is appropriate that costs, if any, associated with the creation of resale competition be recovered from end-users in retail rates.

129 The Act does not require that the ILEC "shed" such costs in order for them to be considered "avoided." If a cost is not incurred to provide wholesale service, then it would not be appropriate to recover that cost from wholesale customers, and that cost should be considered "avoided." For example, the expenses an ILEC incurs in advertising its retail services will not be shed by the ILEC when it begins to provide services for resale, and, in fact, may increase as the ILEC responds to new competition. Yet, such costs are clearly inapplicable to the ILEC's provision of wholesale services, and it would be inappropriate if the ILEC's competitors were required to fund its marketing campaigns. The Act thus explicitly defines such marketing expenses as "avoided costs."

130 Thus, all ILEC costs associated with the following Uniform System of Accounts (USOA) categories should be excluded as avoided costs: Uncollectibles; Marketing Expense; Customer Service Expense; and Billing Expense. That portion of the following accounts which is directly associated with the ILEC's retail operations also should be considered avoided cost: Network Support Expense; Operator Systems Expense (if appropriate); Testing Expense; Plant Operations Administration Expense, Call Completion Services; and Number Services.

131 The portion of the following USOA accounts associated with the ILEC's retail operations should be excluded as avoided costs: General Support Expense; Depreciation Expense; Total Executive and Planning Expense; Total General and Administrative Expense; Operating Federal Income Taxes; Operating State and Local Income Taxes; Operating Other Taxes; Other Interest Deductions; and Total Returns.

service basis) should not be left entirely to individual states. Instead, the Commission should, at a minimum, issue general rules to assist the state commissions in their efforts. First, ILECs should be required to submit cost studies to permit state commissions to quantify ILEC costs associated with their retail offerings. Such cost studies should be available for public review and comment, and the ILEC must bear the burden of establishing the accuracy and reliability of such studies. Second, a discount that does not permit viable competition should be presumed, for purposes of Section 208 complaint proceedings and judicial review of arbitrated and other agreements, not to comply with Sections 251(c)(4) and 252(d)(3).[132] Indeed, if an appropriate model or tool is available or can be developed, the Commission may also wish to consider using that model as an explicit "litmus test" for determining whether a proposed avoided cost discount complies with the requirements of the Act. Analogous to the litmus test approach using the Hatfield Model for TSLRIC pricing of unbundled network elements, a wholesale rate under review by the Commission in enforcement, complaint, Section 271 or other proceedings can be presumed lawful if it is at or below the rate proposed by application of the avoided cost model. A party proposing a different rate would have the burden of proving that such rate better meets the Act's standards.

Finally, the Commission should confirm that the Act does not preclude states from increasing the level of the wholesale discount above that which would be derived based

[132] In this regard, the discount may include an additional amount intended to reflect differences, if any, in the quality of service (including operational interfaces) provided to the reseller compared to what the ILEC provides to its own retail operations. Such amount would be in addition to, not in lieu of, any damages to which the reseller may be entitled under the 1996 Act.

solely on "avoided costs." State commissions retain the authority under Section 261(c) to take additional actions to "further competition" so long as their actions are not inconsistent with the Act or the Commission's regulations. An additional discount that a state finds necessary to make competition viable would not be inconsistent with either the 1996 Act or the Commission's regulations.

V. THE COMMISSION SHOULD ADOPT OTHER RULES REGARDING THE DUTY TO NEGOTIATE IN GOOD FAITH, AVAILABILITY OF AGREEMENTS TO OTHER CARRIERS, AND EXEMPTIONS UNDER SECTION 251(f)(2).

A. Duty Of Good Faith.

The NPRM (¶47) seeks comment on whether the Commission should establish national guidelines regarding the duty imposed under Section 251(c)(1) to negotiate in good faith, and, in particular, "whether certain practices should be deemed to violate" that duty. As with the other duties imposed by Section 251, the Commission has both the right and obligation to establish rules that will facilitate the implementation of the duty to negotiate.

AT&T's experience in negotiating with ILECs both before and after the Act became law, like that of other parties, confirms the wisdom of the Commission's suggestion (id.) that such rules are necessary. AT&T's attempts to negotiate agreements with ILECs have been frustrated by a variety of practices, including refusals to provide information to which other parties are clearly entitled under other provisions of the Act (e.g., interconnection agreements with other parties), or which is relevant to formulating and evaluating proposals (e.g., cost and pricing information).[133] Other ILEC practices which likewise reflect the absence of ALEC bargaining power and are equally disruptive of the negotiating process include an ILEC's failure to respond in a timely manner to an ALEC's proposal, or even to confirm that it is willing to discuss a particular subject.[134]

A clear Commission ruling here that such practices violate the duty to negotiate in good faith could only make the negotiations more productive and efficient.[135] Indeed, whatever minimal progress has been made in the negotiations appears to be attributable almost entirely to the threat of regulatory intervention. The need for such intervention may be eliminated, or at least postponed, by making clear that the following (and similar) practices violate the duty to negotiate in good faith:

- refusal to begin negotiations until unreasonable pre-conditions have been met (e.g., that an entrant limit its legal remedies, be "certified" by the state, or accept a non-disclosure agreement containing terms such as prohibition on disclosure of information to regulatory bodies, courts, or the Department of Justice).

- failure to provide relevant information necessary to allow parties to engage in meaningful negotiations or arbitration (e.g., other interconnection agreements; cost

133 For example, Bell Atlantic has not yet even provided a list of services it proposes to make available for resale, and Ameritech has not provided AT&T any cost studies supporting the wholesale discounts and network element prices it has proposed in negotiations. U S WEST and GTE have not quoted proposed wholesale rates, and refused to provide cost studies. BellSouth is refusing to provide necessary service-specific cost studies and Bell Atlantic and BellSouth have both refused to provide copies of pre-1996 Act interconnection agreements with other LECs.

134 For a variety of reasons -- all unacceptable to AT&T -- AT&T has experienced significant delays in its efforts to conduct meaningful negotiations with several ILECs.

135 The Commission need not, however, adopt a specific definition of "good faith negotiations." The Supreme Court has recognized that a "[s]tatutory standard such as 'good faith' can have meaning only in its application to the particular facts of a particular case." NLRB v. American National Insurance Co., 343 U.S. 395, 410 (1952).

and demand information relevant to pricing of interconnection, network elements, collocation, or wholesale service).

- refusal to commence or participate in negotiations, mediation, or arbitration, with or without the state commission present.
- refusal to negotiate terms for each item listed in Section 251 (and Section 271(c)(2)(B) if applicable).
- refusal to cooperate with the state commission in carrying out its function as a mediator or arbitrator.
- employing dilatory tactics, such as refusing to take a position within a reasonable time in response to a request by the other party.
- failure to confer authority on negotiators to bind the carrier to an agreement.
- refusal to conduct, or delays in conducting, operational readiness testing.

In addition, the Commission should make clear that other conduct or practices may constitute a breach of the duty of good faith under the facts of a particular case.

B. State Approval Of Agreements And Availability To Other Carriers.

Section 252(a)(1) of the Act explicitly provides that "any interconnection agreement negotiated before the date of enactment of [the Act] shall be submitted to the state commission under subsection (e) of this section." Section 252(e)(2)(A), in turn, empowers a state commission to reject such a pre-existing agreement to the extent it discriminates against a telecommunications carrier that is not a party to the agreement. Finally, Section 252(i) mandates that "any interconnection, service or network element provided under an agreement approved under [S]ection [252]" must be made available to any other requesting telecommunications carrier upon the same terms and conditions.

It could not be clearer from these provisions that ILECs who have entered into interconnection agreements with other LECs are required to submit those agreements to the state commissions. More fundamentally, the terms of those agreements must be made available to any requesting carrier without discrimination. Nevertheless, a number of ILECs have refused to submit to the state, or disclose to other parties, their interconnection agreements with other ILECs or even ALECs.

The Commission should therefore confirm that ILECs are obligated to submit these agreements, including those negotiated prior to the Act, to state commissions and make them available to other parties -- as the plain language of the Act requires. The relevance of pre-Act agreements to the clear purpose of the Act is obvious.[136] At a minimum, the terms and conditions under which a large LEC already interconnects with another LEC provide a needed "baseline" for prospective new local competitors -- both in facilitating meaningful negotiations (and providing useful information to state commissions in arbitrating or approving new agreements), and in affording prospective entrants at least the "safety net" of existing terms and conditions while they pursue their own negotiations.

In this regard, it is critical that the Commission not only confirm that ILECs must disclose their existing and future interconnection agreements, but also ensure that "any interconnection, service or network element" provided under such agreement is made available to "any requesting carrier upon the same terms and conditions," as required by Section 252(i). In particular, the Commission should confirm that Section 252(i) requires, at least with respect to arbitrated agreements approved by state commissions under Section 252(e)(2)(B), that an

[136] This is especially so with respect to agreements between ILECs and other LECs in adjacent or nearby territories for the exchange and termination of local and "local toll traffic," and agreements between ILECs and ALECs seeking to compete in the same territory.

ILEC make interconnection, services or network elements provided thereunder available to other carriers on an unbundled basis.[137] Any other result would be contrary to Congress' directive that "any" interconnection, service or network element be made available to other

carriers,[138] would limit the options available to new entrants,[139] and permit the LEC to discriminate between the original and subsequent requesting carriers,[140] all to the detriment of competition and consumers.

C. Rural Carrier Exemption Under Section 251(f)(2).

In order to implement the new "national" telecommunications policy, the obligations of Section 251(b) apply to "each" LEC, and the obligations of Section 251(c) apply to "each" ILEC, subject to an exemption (terminable by the state) in Section 251(f)(1) for "rural telephone companies," as narrowly defined in Section 3(47). Section 251(f)(2),

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137 Because interconnection, services and network elements covered by an arbitrated agreement approved by the State must separately comply with the requirements of Section 251, there is no conceivable basis to require a requesting carrier to accept and pay for services and network elements which the carrier does not need or desires to obtain elsewhere.

138 See Senate Commerce Committee Report, March 30, 1995, at 22. In discussing Section 251(g) of the Senate version of the bill, which became Section 252(i), the Senate Commerce Committee Report states that this section was designed to "make interconnection more efficient by making available to other carriers the individual elements of agreements that have been previously negotiated."

139 Indeed, allowing an ILEC to make services and network elements available to other carriers on a bundled basis only would enable the ILEC to insert into its agreements a "poison pill" containing onerous terms for a service or network element that the original customer does not need, in order to discourage subsequent carriers from making a request under that agreement.

140 See Senate Commerce Committee Report, March 30, 1995, at 22. ("The Committee intends this requirement to help prevent discrimination . . . .")

however, permits a state to suspend or modify these obligations in response to the petition of a LEC with fewer than 2% of the Nation's subscriber lines, provided that such LEC is able to show that such suspension or modification is "necessary to avoid a significant adverse impact" on consumers, or would cause "undue economic burden" on the LEC, and is otherwise consistent with the public interest.

Although state commissions are responsible for deciding whether a petitioning LEC has satisfied the criteria of Section 251(f)(2), pursuant to its authority under Section 251(d), the Commission can and should establish a few limited standards to guide the states in their review of such petitions. At a minimum, the Commission should require that the 2% threshold for filing a petition under Section 251(f)(2) be applied at the holding company level, not to individual operating companies. Any other interpretation would allow the RBOCs, GTE and Sprint to insulate sections of their large, and often contiguous, monopolies from competition by claiming that they are "rural carriers" entitled to "suspension" of their obligations under the Act.[141]

The Commission should also make clear that Section 251(f)(2) must, consistent with Supreme Court precedent,[142] be narrowly construed, and that it may not be used to allow

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141 AT&T estimates that more than 115 operating companies of the RBOCs, GTE and Sprint could apply for an exemption under Section 252(f)(2) -- and thereby make a mockery of the Act's core goal -- if the 2% test is applied at the operating company level rather than the holding company level. See Universal Service Fund Data Request, CC Docket No. 80-286 (1994) (data drawn from 1993 data filed by parties to proceeding on March 1, 1995).

142 To safeguard the congressional commitment to competition which underlies the antitrust laws, the Supreme Court has repeatedly held that express and statutory exemptions from the antitrust laws must be construed narrowly. See, e.g., Union Labor Life Ins. Co. v. Pireno, 458 U.S. 127, 136, 102 S.Ct. 3002, 3007 (1982); Group Life Health Ins. Co. v.

(footnote continued on following page)

LECs to "opt out" of the regulatory and policy framework that Congress has mandated. LECs with less than 2% of subscriber lines include state-wide carriers such as SNET,[143] and other major Tier 1 carriers, such as Cincinnati Bell and Rochester Telephone, earning hundreds of millions of dollars in annual revenues. The Act presumes that, in contrast to the smaller "Rural Telephone Companies" that are exempt under Section 251(f)(1), these carriers are no less capable of complying with Section 251(b) and (c) than carriers with more than 2% of subscriber lines, and that competition in the territories served by these carriers will further the public interest.

To ensure that Section 251(f)(2) is not abused, the Commission should make clear that the statutory criteria must be stringently applied. At a minimum, the Commission should require that a petitioning carrier demonstrate that the application to it of the Section 251(b) or (c) obligations that are the subject of its petition would inflict substantial harm on the LEC and customers in its territories that would not be inflicted on larger LECs

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Royal Drug Co., 440 U.S. 205, 231, 99 S.Ct. 1067, 1083 (1979); Abbott Laboratories v. Portland Retail Druggists Assn., Inc., 425 U.S. 1, 11, 96 S.Ct. 1305, 1313 (1976). The reasoning in these cases applies equally to the Act, which is similarly designed to promote competition.

143 The Southern New England Telephone, ("SNET") has approximately 360 subscriber lines per square mile (see USF Data Request, CC Docket No. 80-286 (1994)), had $1.472 billion in net revenues in 1995 (see SNET ARMIS Quarterly Report 43-01, April 1, 1996, Table 1), and provides service in a state that has one of the highest per capita incomes in the United States (see *Statistical Abstract of the United States*, p. 41, Table 2 (1995)). SNET has applied for an exemption under Section 251(f)(2). See Petition of Southern New England Telephone Company, Application of the Southern New England Telephone Company for Suspension of Section 251(c)(4) of the Telecommunications Act of 1996, Docket No. 96-03-19 (State of Connecticut, Department of Public Utility Control).